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No. 95-445

IN THE
Supreme Court of the United States
OCTOBER TERM, 1995

ERNST & YOUNG LLP,
Petitioner,

v.

RHODE ISLAND DEPOSITORS ECONOMIC PROTECTION CORPORATION, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the Supreme Court of Rhode Island

PETITIONER'S REPLY MEMORANDUM

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PETITIONER'S REPLY MEMORANDUM

The briefs of DEPCO and the receivers ("DEPCO Br.") and of the Brown credit union directors ("Dir. Br.") attempt to obscure the central point of Ernst & Young's petition: by upholding the Act, the Rhode Island Supreme Court held, in substance, that a state may change the rules in the middle of a lawsuit between the state and a private party, and thereby deprive the private party of a recognized property interest, for no better reason than to improve the state's own position in the lawsuit. We are aware of no authority — and respondents have cited none — suggesting that this kind of blatant attempt to tilt the scales of justice in favor of the state is consistent with due process.

1. In their effort to articulate a legitimate purpose for the Act, respondents suggest that the Act was necessary to protect settling defendants from contribution claims and thereby encourage settlements. But in doing so, respondents have misrepresented both the effect of the Act and the law in Rhode Island as it existed before the Act was adopted.

a. Respondents suggest that the prior law (which is still in effect for all but the small number of cases governed by the Act) "imped[ed] settlement" because, "as a general rule," settling parties remained "potentially liable to other defendants" for contribution, which "ma[de] it impossible for one tortfeasor alone to take a release and close the file." DEPCO Br. 11, 3, 10. In fact, there never was any "general rule" that settling parties would remain liable for contribution in Rhode Island. To the contrary, the prior law clearly provided that settling defendants could be shielded from contribution, at the plaintiff's option, so long as the non-settling defendants were released from the settling party's proportionate share of liability. *See* R.I. Gen. Laws 10-6-8. The Act did not change the availability of contribution protection for settling parties; it changed the type of set-off provided to *non*-settling parties. Under the Act, the liability of non-settling parties is reduced by the amount of the settlement (*pro tanto*), rather than by the settling party's proportionate share of liability.

Thus, the notion that the Act was needed to protect settling parties from contribution claims is a fiction. Under the prior law, plaintiffs (including DEPCO) always had the ability to provide settling parties with such protection. DEPCO was not unable to protect settling parties from contribution claims; it merely chose not to do so.[1]

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[1] The notion that settlement efforts were unsuccessful because DEPCO "would not agree to provide unlimited indemnification" to settling

b. Respondents suggest that the "principal thrust" of the Act was to "adjust potential liability among the various tort-feasors . . . not among DEPCO and the defendants." DEPCO Br. 12. In fact, the opposite is true. The Act takes rights away from non-settling parties such as Ernst & Young, but (as noted above) it does not give settling defendants anything they could not have been given under prior law. Instead, the beneficiary of the Act is DEPCO. DEPCO can now achieve the same result it could have achieved under the prior law — encouraging settlements by offering contribution protection to settling parties — but it can do so without having to provide proportionate fault releases to non-settling defendants.

It is true, as respondents contend, that under the prior law, DEPCO (like every other plaintiff) had to accept the risk that entering into inadequate settlements with settling defendants would leave it "at risk of insufficient recovery." DEPCO Br. 11. Indeed, that is precisely our point. The effect of the Act is to shift the risk that DEPCO will enter into inadequate settlements away from DEPCO itself and onto Ernst & Young — and to do so retroactively, in the middle of litigation between DEPCO and Ernst & Young.

c. The fact that other jurisdictions have adopted *pro tanto* contribution rules as generally applicable law, or that Congress has properly enacted retroactive tax measures in some cases, in no way suggests that the Act is consistent with due process. Unlike the Act, the application of these statutes does not depend on the identity of the plaintiff, nor were

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parties (Dir. Br. 5) is incorrect. There was no need for indemnification under the prior law, because DEPCO could provide contribution protection by offering non-settling parties a proportionate share release. This is not, as respondents would have it, Ernst & Young's "own solution to the problem" (DEPCO Br. 11): it is the solution that was provided by Rhode Island law.

these statutes enacted for the purpose of affecting pending litigation involving the state. None of these general laws, in short, comes with the baggage that renders the Act infirm.

We do not contend that a legislature could not constitutionally decide, as a matter of general policy, that non-settling alleged tortfeasors, rather than plaintiffs, should bear the risk of inadequate settlements.[2] We do contend, however, that a state legislature may not *retroactively* reallocate that risk in a manner that benefits a state entity in its litigation against a non-settling defendant, and that deprives the defendant of an existing property interest recognized by state law.

2. The record amply supports Ernst & Young's contention that it was the intended target of the Act. As we noted in our petition, DEPCO's trial counsel argued before the legislature that the Act's purpose was to force Ernst & Young to settle the lawsuit brought by DEPCO, and that the law should be changed only in his litigation to benefit his client. Pet. 7. We noted that DEPCO's counsel had not denied making such statements, and had offered no evidence to rebut the affidavit

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[2] It is of course true that *McDermott, Inc. v. AmClyde*, 114 S. Ct. 1461 (1994), in which this Court unanimously adopted the proportionate fault approach for admiralty cases, does not mean that a state is precluded from adopting a different approach. *McDermott* does, however, undercut the notion that a statute abandoning the proportionate fault approach in favor of a *pro tanto* rule is rationally related to the purpose of facilitating settlements. *See id.* at 1468, 1469 (*pro tanto* rule has "no clear advantage in promoting settlements," and any pressure to settle resulting from that rule is "unnecessary" and "comes at too high a price in unfairness").

on these points presented by Ernst & Young. *Id.* n.2.[3] Having now had an additional opportunity to take direct issue with these statements in their brief, DEPCO's counsel *still* has not done so. Instead, DEPCO argues that the court below "necessarily and properly rejected" the contention that the Act targeted Ernst & Young. DEPCO Br. 14 n.15. That is simply not true, as even a cursory reading of the opinion below makes clear. The court merely held that the Act was not intended to *punish* Ernst & Young within the meaning of the bill of attainder clause. Pet. App. 19a.

In fact, as we noted in our petition, it was a matter of public knowledge that the Act was targeted at Ernst & Young. Pet. 7. Respondents do not even try to explain why, if the notion that Ernst & Young was the target of the Act is a fantasy, two writers for two Rhode Island newspapers who followed the proceedings in the Rhode Island legislature apparently suffered from the same delusion.

There is a simple reason why the Act was directed at Ernst & Young. Although there are many other parties who are potentially liable for the "credit union crisis" — in particular, officers and directors of RISDIC and the credit unions, who had direct responsibility for managing the institutions (unlike Ernst & Young, which merely served as outside auditor for some of the institutions in certain years) — Ernst & Young is the only large, national, "deep pocket" defendant. DEPCO's strategy, as we noted in the court below, has been to attempt to settle cheaply with the other defendants and

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[3] The affiant was a senior lawyer for Ernst & Young who followed the legislative proceedings and was familiar with the arguments made by DEPCO's counsel. It is noteworthy that, having had a clear opportunity to deny making the statements in question, DEPCO's counsel instead chose to comment on the source of the affidavit. *See* DEPCO Br. 14 n.15.

then to coerce Ernst & Young into a large settlement by threatening to hold it liable for the shortfall. *See* Affidavit of William P. Hammer ¶ 5, submitted in the proceedings below. The Act made this strategy possible.[4]

3. The conflict between the decision below and the Supreme Court of Virginia's decision in *Shiflet v. Eller*, 228 Va. 115, 319 S.E.2d 750 (1984), is quite real. If there were any doubt about the meaning of *Shiflet* when that case was decided, that doubt was erased by the same court's decision a year later in *Potomac Hospital Corp. v. Dillon*, 229 Va. 355, 329 S.E.2d 41, *cert. denied*, 474 U.S. 971 (1985). In that case, the court characterized *Shiflet* as holding not that a retroactive abrogation of a right to contribution is prohibited by Virginia *statutory* law, but that such an action *"violates due process and is therefore unconstitutional."* *Id.* at 360, 329 S.E.2d at 44-45 (emphasis added).

Respondents fail to mention *Potomac Hospital*. They also fail to note that the *Shiflet* court cited not only two state cases on statutory construction, but also a federal court decision from Virginia, *Carickhoff v. Badger-Northland, Inc.*, 562 F. Supp. 160, 164-165 (W.D. Va. 1983), in which the court held that the retroactive abrogation of a right to contribution violated the federal due process clause.[5] The citation to

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[4] To this extent, it might indeed be said that the Act promotes settlement by threatening non-settling parties with enormous and disproportionate liability. *See* Dir. Br. 5, 12. As we noted in our petition, however, depriving Ernst & Young of a property interest in order to coerce Ernst & Young into a settlement cannot constitute a rational means of furthering a legitimate purpose. Pet. 16-17.

[5] Although the citation to *Carickhoff* makes reasonably clear that *Shiflet* was based upon the federal due process clause, it does not matter whether the Court had the federal or the state clause in mind: they are

Carickhoff makes clear that, as the court itself later held in *Potomac Hospital*, *Shiflet* is a due process decision. Whether *Shiflet* arguably *could* have been decided on purely statutory grounds is beside the point.

4. The failure of the Act, as interpreted by the Rhode Island Supreme Court, to afford non-settling parties a meaningful opportunity to participate in settlement proceedings affecting their rights provides an additional and independent basis for this Court to grant certiorari.[6] Respondents' argument that Ernst & Young was permitted to file a brief and appear at a hearing in connection with the Brown settlement — and that "the cases cited by [Ernst & Young] call for nothing more" than this (DEPCO Br. 16; *see also id.* at 9) — is false. In fact, the cases cited in our petition require substantially more than the limited participation afforded to Ernst & Young. These cases are in direct conflict with the result in the court below.

For instance, in *In re Jiffy Lube Securities Litigation*, 927 F.2d 155 (4th Cir. 1991), the court held that where a settlement exposes the non-settling defendant to excess liability — as the Brown settlement did — the non-settling party must be

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coextensive. *See* Pet. 19 n.5, citing *Leftwich v. Bevilacqua*, 635 F. Supp. 238, 243 (W.D. Va. 1986).

[6] Respondents' weak suggestion that this argument might not have been preserved in the trial court (DEPCO Br. 16 & n.17) is meritless. *None* of the constitutional arguments was briefed in any detail in the trial court: that was one reason why Ernst & Young argued that the court below should not decide the constitutional issues. *See id.* at 5. Nevertheless, the Rhode Island Supreme Court accepted the certified questions from the trial court — including "[w]hether the [Act] violate[s] the Due Process Clause of the Fourteenth Amendment" (Pet. App. 1a) — and addressed those questions in a legally binding opinion. The present issue was fully addressed by both sides in the proceeding below.

permitted to participate not just in *some* hearing, but in a hearing that "focus[es] on [the] *fairness of the settlement to the non-settling defendant.*" *Id.* at 160 n.3 (emphasis added). *Accord In re Del-Val Fin. Corp. Sec. Litig.*, 868 F. Supp. 547, 559 (S.D.N.Y. 1995); *see also Bragger v. Trinity Capital Enter. Corp.*, No. 92 Civ. 2124, 1993 U.S. Dist. LEXIS 10087, at *6 (S.D.N.Y. July 23, 1993) (court considered deposition transcripts and other evidence offered at hearing in considering fairness of settlement to non-settling parties).

Respondents' contention that *Jiffy Lube* imposes no special duty of fairness to non-settling parties (Dir. Br. 16) is a complete misreading of the case. The *Jiffy Lube* court did say that if the non-settling party is given a *proportionate share* set-off — the type of set-off to which Ernst & Young would be entitled were it not for the Act — then the non-settling party would be entitled only to a basic right to be heard. But the court also made it clear that if the non-settling party receives only a *pro tanto* set-off — the type of set-off provided by the Act — then "a separate hearing on fairness *from the perspective of the non-settling defendant*" is required. *Jiffy Lube*, 927 F.2d at 160 & n.3 (emphasis added).

Girsh v. Jepson, 521 F.2d 153 (3d Cir. 1975), confirms that merely filing a brief and taking part in a hearing does *not* amount to the kind of meaningful participation in the process to which a non-settling party is entitled under a *pro tanto* set-off scheme such as the Act. In *Girsh*, the trial court permitted an objector to a settlement to do both of these things. (Moreover, like Ernst & Young here, the objector had obtained a brief extension of time in order to do so.) However, the court rejected the objector's complaints about the "sparseness of the record," and denied her efforts to obtain information from the settling parties relevant to the reasonableness of the settlement. *Id.* at 156, 157. On these facts, the Third Cir-

cuit reversed the trial court's approval of the settlement. It concluded that the objector had not been given "an opportunity for *meaningful* exposition" of her position because she was "not afforded an adequate opportunity to test" the "strengths and weaknesses" of the settlement. *Id.* at 160, 157 (emphasis added). In addition, the court found that the trial court had erred by not "evaluat[ing] all the contentions of the parties," including the objector. *Id.* at 160.

What happened in the trial court in *Girsh* is precisely what happened to Ernst & Young in the *Brown* matter. Ernst & Young was allowed to file a brief and attend a hearing, but was denied the opportunity to obtain and present evidence relevant to the fairness of the settlement. *See* Pet. 22.[7] Moreover, the court did not consider whether the settlement would improperly infringe on the rights of third parties such as Ernst & Young. It approved the settlement as "in the best interests of *the moving parties and the receivership estates*" (Pet. App. 26a) (emphasis added), but it made no mention of whether the settlement adequately protected Ernst & Young's interests.

Thus, like the objector in *Girsh*, Ernst & Young did not receive the *meaningful* opportunity to participate that is

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[7] Respondents make much of the notion that Ernst & Young had received "massive discovery" in the overall credit union litigation. DEPCO Br. 5 n.6; *see also* Dir. Br. 16. In fact, there had been very little discovery relating to the Brown credit union. At the time that DEPCO and the credit union receiver made their files available for inspection by Ernst & Young, the case that was eventually settled — DEPCO's suit against the Brown directors — did not exist. Moreover, Brown was not, and was unlikely to become, a focus of DEPCO's suit against Ernst & Young. (Ernst & Young never issued any audit report on Brown.) It was only after the document discovery in question was completed that the Brown complaint was filed and Ernst & Young brought in as a third-party defendant.

required under federal case law. The Rhode Island Supreme Court's affirmance of the settlement — confirming the trial court's interpretation of what the Act requires for the approval of a settlement — makes clear that the Act is at odds with *Girsh* and other federal decisions.

For the foregoing reasons, and for the reasons stated in the petition, the petition for a writ of certiorari should be granted.

Respectfully submitted.

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